



Property Casualty Insurers
Association of America
Shaping the Future of American Insurance

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STATEMENT

PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA (PCI)

H.B. 6280 – AN ACT EXTENDING THE SUNSET DATE FOR PERSONAL RISK INSURANCE RATE FILINGS

INSURANCE AND REAL ESTATE COMMITTEE

February 19, 2009

The Property Casualty Insurers Association of America (PCI) appreciates the opportunity to comment on H.B. 6280. Our comments are provided on behalf of the member companies of PCI, a national property casualty trade association with over 1,000 member companies. PCI member companies provide almost 50 percent of Connecticut's personal auto coverage.

PCI strongly supports H.B. 6280, which would extend the state's flex rating law affecting personal lines until July 1, 2011. The law went into effect on July 1, 2006 and is scheduled to sunset on July 1, 2009. Under the law, insurance companies in Connecticut are allowed to implement personal auto and homeowners' insurance rate changes within a ± 6 percent band without waiting for regulatory approval.

Because the flex-rating program is still relatively new in Connecticut, insufficient time has elapsed for recent comprehensive data to be compiled to examine its true effectiveness. However, the information that is available does suggest that the law is operating as intended, moderating premium costs and contributing to a vibrant, competitive market.

Under flex-rating, policyholders benefit from a market environment characterized by healthier competitive forces and flexibility, and which does not jeopardize consumer protections. This type of system allows insurers greater flexibility in responding to competitive market conditions and adjusting certain rates more quickly in accordance with the changing loss experience. Thus, flexible rate revisions under this mechanism are not as volatile as rates that require prior approval. Regulators can also free up some of their time for other important duties such as overseeing market conduct, monitoring potential insolvencies and providing consumer education.

Premium Adjustments Benefit Consumers

Based on companies' experience, the trend in Connecticut's personal auto liability premiums relative to the trend in liability losses suggests that recent rate changes have been lower than changes in losses since flex-rating went into effect. For example, although the loss cost increased 4.2 percent from 2007 through the third quarter of 2008, the rate has not increased commensurately; the data instead suggest that the price went down 2.4 percent during this time. On the other hand, prior to flex-rating, rate adjustments were higher than loss cost trends. For example, the average liability premium rose 1.9 percent while losses fell 2.0 percent from 2003 to 2004. Premiums and losses decreased at about the same pace from 2004 to 2005 (2.6 percent and 2.9 percent, respectively).

The lower rate adjustment relative to the loss pattern from 2007 through September 2008 is due in part to the elimination of the additional underwriting risk inherent within a prior approval system. Since prior approval often creates a delay in the review process, companies are hesitant to lower rates for fear that they will not be able to increase them when needed later. The fact that the rate appears to have fallen during the latest period while the loss cost rose suggests that Connecticut drivers are benefiting from the flex-rating program.

The Connecticut Personal Auto Market Remains Competitively Strong

The structure of an insurance market can be described in terms of (1) the number of insurers; and (2) the relative market power of leading insurers. If there are many sellers of insurance and if the market shares of the largest insurers are relatively small, a market is considered competitive since sellers are forced to set prices at the lowest possible level in order to attract and hold customers.

Number of Insurers: Insurers are constantly entering and leaving particular insurance markets so that the number of companies active at any given time is in flux. The greater the number of active competitors in a market, the stronger the presumption of sufficient competition. According to data compiled by the National Association of Insurance Commissioners (NAIC), there are 152 personal auto carriers operating in Connecticut. This figure is equivalent to the average number writing in other states in the nation, indicating that there is a wide variety of companies offering auto insurance in Connecticut.

Market Power: Theoretically, if one or a few firms control unreasonably large shares of the market, then prices and availability might be unduly influenced by the actions of the leading firms. In its guidelines for analyzing the economic impact of proposed mergers, the United States Department of Justice recommends that market power be measured using the Herfindahl-Hirschman (i.e., Herfindahl) index. This index is superior to evaluating market shares of only the top writers because it considers both the total number of sellers in the market and their relative sizes.

Markets with index values less than 1,000 are considered “unconcentrated;” markets with values between 1,000 and 1,800 are considered “moderately concentrated;” and markets exhibiting values greater than 1,800 are considered “highly concentrated.” The closer a market is to being non-competitive, the higher the market’s concentration. The computed Herfindahl index for the Connecticut personal auto line is 270, which is significantly lower than the 1,000 threshold. In other words, a very unconcentrated (i.e., competitive) auto insurance market is found to exist in this state.

Conclusion

Congressional leaders calling for more modernized insurance regulation have cited “speed-to-market” and competition-based pricing as crucial elements in regulatory modernization. Thirty-seven states, including Connecticut, have enacted less restrictive regulatory systems with flex rating laws in 8 states and “file and use”, “use and file” or “no-file” laws found in 29 states. Only 13 states operate under a prior approval law or use rates developed by the state. The national trend is clearly in the direction of more competitive systems. Within the last few years, Alaska, Connecticut, Louisiana, Nebraska, New Mexico, North Dakota, Oklahoma, Rhode Island, Texas, and Georgia have moved to less restrictive rating laws. And just last year, New York moved from a prior approval to a flex rating system. Flex-based rates make it possible for insurance companies to compete more vigorously and swiftly on price. Modernization of insurance rates is a key element to preserving state regulation of insurance, and Connecticut lawmakers can play a key role in ensuring that modernization continues to be in place to benefit the insured drivers of the state.